No. 22,234

IN THE

United States Court of Appeals

For the Ninth Circuit

ADELINE FRASCH,
Appellant,

vs.

THOMAS C. WILSON and SALLY B. WILSON,
Appellees.

APPELLANT'S OPENING BRIEF

BRADLEY, WAGY, BUNKER, HISLOP & GIBBONS,
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APPELLANT'S OPENING BRIEF

I. A STATEMENT OF THE PLEADINGS AND THE FACTS GIVING JURISDICTION TO THE DISTRICT COURT AND TO THIS COURT

In 1966 Thomas C. Wilson and Sally B. Wilson filed a petition in bankruptcy in the United States District Court, Central District of California. (R. 26) On November 29, 1966 John P. Stodd, trustee in bankruptcy for the Wilsons, applied to Robert B. Powell, referee in bankruptcy for the U.S. District Court, for an order requiring appellant Adeline Frasch to turn over to trustee Stodd a note and trust deed executed by R. A. Diedrich and V. J. Shrader payable to the bankrupts and given by the bankrupts to Mrs. Frasch as security for her loan to Thomas C. Wilson of $7,000.00. (R. 2; R. 14)

Without a hearing and in the absence of Mrs. Frasch and her attorney, the referee in bankruptcy, Robert B. Powell, decreed that he had summary jurisdiction to hear and decide Mrs. Frasch's rights to the note and trust deed which she held. (R. 7)

He continued the matter until February 1, 1967 and at that time took the matter under submission. He made a memorandum opinion on February 24, 1967 (R. 24), and findings of fact and conclusions of law and a turnover order on March 30, 1967. (R. 35)

A petition for review was then timely filed in the United States District Court, Central Division under Section 39(c) (11 U.S.C.A. 67-c) of the Bankruptcy Act. (R. 36)

An order affirming the referee's order was made by the District Court on the 21st day of July 1967 (R. 45); and a notice of appeal to this court was filed by appellant on August 11, 1967 under the provisions of the Bankruptcy Act Sections 24 and 25 (11 U.S.C.A. 47 and 48). (R. 47)

II. STATEMENT OF THE CASE

On August 6, 1964 R. A. Diedrich and V. J. Shrader gave Thomas C. Wilson and Sally B. Wilson a note for $9,742.61 secured by a trust deed. (R. 13)

On September 28, 1964 appellant Adeline Frasch loaned Thomas C. Wilson $7,000.00, and Thomas C. Wilson and Sally B. Wilson gave her the Diedrich and Shrader note and trust deed as collateral security

for Thomas C. Wilson's note for $7,000.00. (Referee's finding of fact III, R. 27)

The Diedrich and Shrader note and trust deed were thereby pledged to Adeline Frasch. (Referee's memorandum opinion, R. 24)

On March 26, 1966 the Wilsons were adjudicated bankrupt. (R. 27)

On November 29, 1966 John P. Stodd, trustee in bankruptcy for Thomas C. Wilson and Sally B. Wilson, applied to Robert B. Powell, referee in bankruptcy for the U. S. District Court, Central Division of California, for an order requiring Adeline Frasch to turn over to trustee Stodd the note and trust deed. (Trustee's application for Turnover order, R. 2)

On December 9, 1966 referee Robert B. Powell ordered Adeline Frasch to appear before him on December 20, 1966 to show cause why she should not be ordered to turn over the Diedrich and Shrader note and trust deed. He ordered her to file and serve an answer on trustee John P. Stodd's attorney, Gilbert Mueller, at least two days before the hearing. (Referee's Amended Order to show cause, R. 5)

The sheriff served this order on Mrs. Frasch at noon December 15, 1966. (Answer R. 10)

Because there was not enough time to prepare and serve and answer, Mrs. Frasch's attorney, Phillip Wagy, called Gilbert Mueller's office and asked for and obtained an unqualified agreement that the entire matter would be continued. (Answer, Affidavit of Phillip Wagy, R. 17)

The matter was thus continued by "telephonic request of respondent's attorney to February 1, 1967". (Referee's findings of fact, R. 26)

Relying on this continuance, neither Mrs. Frasch nor her attorney appeared at the hearing originally set for December 20, 1966. (R. 26) However, John P. Stodd, the trustee and Gilbert Mueller, his attorney, did. (R. 26)

In the absence of Mrs. Frasch and her attorney and without any hearing whatsoever, Mr. Stodd and Mr. Mueller obtained, and Robert B. Powell, the referee, signed an order decreeing that Mr. Powell, the referee, had summary jurisdiction to hear and to decide the rights of Mrs. Frasch to the note and trust deed which she had in her possession. (Referee's order for Continuance and in re summary jurisdiction, R. 7)

Believing that the order in re summary jurisdiction was made without due process, Mrs. Frasch did not ask for a review, but asked the referee to correct this error. (R. 11)

On February 1, 1967 and within the time set by the continuance Mrs. Frasch objected to the summary jurisdiction of the court and asserted her rights as a secured creditor. (Answer R. 9, Points and Authorities R. 20)

The referee made his memorandum opinion on February 24, 1967 (R. 24) and his findings of fact and conclusions of law on March 30, 1967 (R. 26) his conclusions of law being:

I.

Since no appeal has been taken within the time prescribed by law, from the Court's order of summary jurisdiction, said order is final, and this Court has summary jurisdiction over this matter.

II.

That the filing of a continuation statement by respondent was mandatory as required by Section 10102 (c) of the California Commercial Code in order to perfect her interest in the note and trust deed signed by R. A. Diedrich and V. J. Shrader which was collateral security for the note executed by bankrupt Thomas C. Wilson to respondent.

III.

This respondent is a general unsecured creditor of this bankrupt estate and its claim of lien against the subject note is null and void.

III. SUMMARY OF ARGUMENT

The question presented is whether or not the above conclusions of law are wrong. Mrs. Frasch says indeed they are, and presents her argument as summarized:

A.

The referee had no jurisdiction over the Diedrich and Shrader note in Mrs. Frasch's possession. His assumption of jurisdiction was without due process and void. Mrs. Frasch did not consent to his assump-

tion of such summary jurisdiction by not asking for review of this void order.

B.

The filing of a continuation statement by Mrs. Frasch was *not* required by Section 10102 (c) of the Commercial Code of the State of California in order to perfect her interest in the note and trust deed signed by R. A. Diedrich and V. J. Shrader and pledged to her by the bankrupts.

C.

Having a perfected interest in the note and trust deed Mrs. Frasch is a secured creditor and her lien against the pledged note and trust deed is good and valid, and the trustee is entitled to the note and trust deed only on payment to Mrs. Frasch of the debt secured by their pledge.

IV. ARGUMENT

A. THE REFEREE HAD NO JURISDICTION OVER THE DIEDRICH AND SHRADER NOTE AND TRUST DEED IN MRS. FRASCH'S POSSESSION. HIS ASSUMPTION OF JURISDICTION WAS WITHOUT DUE PROCESS AND VOID. MRS. FRASCH DID NOT CONSENT TO HIS ASSUMPTION OF SUMMARY JURISDICTION BY NOT ASKING FOR A REVIEW OF HIS VOID ORDER.

A-1. The referee had no jurisdiction over the Diedrich and Shrader note and trust deed in Mrs. Frasch's possession.

The Diedrich and Shrader note was in Mrs. Frasch's possession. (R. 2) As the court knows:

> "There is hardly any question of law better settled than that a court of bankruptcy has no juris-

diction without the consent of the adverse claimant to hear and adjudicate in a summary proceeding a controversy as to the title of or claims upon property held adversely to the bankrupt estate where such property came into the claimant's possession prior to the bankruptcy."

Vol. 2 Collier on Bankruptcy 14th Ed. page 491.

See:

Suhl v. Bumb, 348 F.2d 869.

"If the property is in the possession of the claimant, his claim is adverse whether he claims to hold an absolute title to such property or only asserts a lien upon it."

Collier, supra, page 498.

A pledgee in possession prior to bankruptcy is an adverse claimant subject only to a plenary suit to determine his interest.

Collier, supra, page 501;

Walker v. Commercial Bank of Little Rock (C.A. 8th 1954) 217 F.2d 677;

Southwestern Lumber Co. of N.J. v. Kerr (D.C. Texas) 29 Am. B. R. (NS) 404, 11 F.Supp. 253, aff'd (C.C.A. 5th Cir.) 78 F.2d 348, Cert. den. 296 U.S. 661, 56 S.Ct. 130, 80 L.Ed. 433;

Seeman v. Nat. Bank of Commerce (C.C.A. 5th 1940) 42 Am. B. R. (NS) 852, 112 F.2d 378.

The trustee cannot establish "constructive possession" of a chose in action represented by an indispensable instrument in the possession of the claimant.

Where a chose in action is represented by a physical document which has been delivered by the bankrupt before bankruptcy to an adverse claimant, summary proceedings are unavailing.

Matter of Republic Plumbing Supply Corp., 295 Fed. 573;

Southwestern Lumber Co. of N.J. v. Kerr (supra);

Seeman v. National Bank of Commerce (supra).

See:

2 Collier on Bankruptcy 14th Ed. pp. 488, 489, 323.05.

See *Pasadena Investment Co. v. Weaver,* 376 F.2d 175 at 178 where the court points out the distinction between a lien holder in possession and one not in possession.

A-2. The referee's assumption of jurisdiction was without due process and void.

It is true that in all proceedings to recover summarily the possession of property from the hands of third persons, a referee has preliminary jurisdiction to inquire into the nature of the defendant's possession and into any adverse claim so far as to see whether it is more than colorable.

Vol. 2 Collier on Bankruptcy 14th Edition 521.

But what did the referee do here? He did not make any inquiry into the nature of Mrs. Frasch's claim on December 20, 1966. He simply and arbitrarily de-

creed that he had summary jurisdiction to hear and decide this matter. (R. 7) He did this apparently on the basis that no answer or objection to the court's jurisdiction had been filed. (R. 7)

The only reason that no answer or objection to the court's jurisdiction had been filed is that Mr. Stodd, the trustee and Mr. Mueller, his attorney had agreed that Mrs. Frasch's attorney could have a continuance. (R. 17) The matter had been continued "by telephonic request of respondent's attorney to February 1, 1967." (Findings of fact and conclusions of law, R. 26)

Having been granted a continuance, naturally Mrs. Frasch and her attorney did not appear on December 20, 1966.

Having agreed to this continuance, Mr. Stodd and Mr. Mueller then obtained an order in the absence of Mrs. Frasch and her attorney on one of only two issues in the case, although both such issues were completely interlocking.

The only basis the trustee claims for jurisdiction is that Mrs. Frasch's claim is merely colorable because she did not file a continuation statement. But the issue of the requirement for filing a continuation statement was continued to February 1. Without deciding that issue, the court had no basis on which to make a finding that it had summary jurisdiction.

And yet the court decreed that it had summary jurisdiction without any hearing of any sort, and in the absence of Mrs. Frasch and her attorney induced by

the agreement of the trustee and his counsel that the matter would be continued.

It has been widely and wisely held that a judgment obtained in a manner preventing a party from having a fair opportunity to present his case is void and may be collaterally attacked.

49 C.J.S. 859 et seq.

Regardless of the means which brought about this miscarriage of justice and deprivation of fair play, there can be no doubt that the assumption of jurisdiction by the referee deprived Mrs. Frasch of a hearing and of due process, and such assumption of jurisdiction is void. "In all cases the claimant is entitled to be heard."

Collier, supra, page 522;
Bradley v. St. Louis Terminal Warehouse (C.A. 8th 1951) 189 F.2d 818;
In re Bacon, 210 Fed. 129;
In re Maki, 14 F.2d 626;
In re Rosser, 101 Fed. 562.

A-3. Since the referee's assumption of summary jurisdiction was void, Mrs. Frasch was not obliged to appeal it, and not requesting a review is not a consent to his void jurisdiction.

See

Bradley v. St. Louis Terminal Warehouse (supra).

Pasadena Investment Co. v. Weaver, 376 F.2d 175 cited by the Honorable Thurmond Clarke (R. 46) is good law but completely distinguishable from the case before him and before this Court.

In that case the Pasadena Investment Company did not object to the referee's assumption of jurisdiction. Mrs. Frasch was deprived of the opportunity to object; the ruling was made when she and her attorney were led to believe the matter was continued.

The *Pasadena* case discusses Rule 2(a) (7) of the Bankruptcy Act as amended 11 U.S.C.A. 11(a) (7) which says in part:

> ". . . and where in a controversy arising in a proceeding under this title an adverse party does not interpose objection to the summary jurisdiction of the court of bankruptcy, by answer or motion filed before the expiration of the time prescribed by law or rule of court or filed or extended by order of court for the filing of an answer to the petition, motion or other pleading to which he is adverse, he shall be deemed to have consented to such jurisdiction."

Mrs. Frasch filed her answer objecting to jurisdiction within the time fixed by order under the agreed continuance; but the court without allowing her to get in her answer or to be heard, made a finding that it had summary jurisdiction.

The trustee's position seems to be that you can agree to give the claimant's attorney an extension of time in which to answer, but then, you can settle one of the issues on the grounds he didn't answer on the date from which you gave him the continuance. This is like giving an attorney a ten day extension to answer a complaint and then taking a default on the day after the answer was originally due. It is far far from due process of law.

The *Pasadena* case does not discuss this issue of due process and the right to be heard; but that is the basis for Mrs. Frasch's asking this Court to hold the referee's assumption of jurisdiction void.

In the *Pasadena* case the appellant had a full three day hearing. Mrs. Frasch had none. Surely Rule 2(a)(7) was not intended, nor should it be interpreted to subvert the constitutional rights of litigants, or to make void proceedings valid.

B. FILING OF A CONTINUATION STATEMENT BY MRS. FRASCH WAS NOT REQUIRED BY SECTION 10102(c) OF THE COMMERCIAL CODE IN ORDER TO PERFECT HER INTEREST IN THE NOTE AND TRUST DEED SIGNED BY R. A. DIEDRICH AND V. J. SHRADER AND PLEDGED BY BANKRUPTS.

B-1. The transfer of the Diedrich and Shrader note and trust deed to Mrs. Frasch by the bankrupts met all the requirements of a valid pledge.

The referee admits this transfer was a pledge. (R. 24) The trustee and referee admit that the Diedrich and Shrader note and trust deed were received by Mrs. Frasch as security. (R. 2; R. 27)

> "A pledge of the Diedrich and Shrader note to Mrs. Frasch took place on September 28, 1964. It was governed by the law effective prior to the adoption of the Uniform Commercial Code in California, effective January 1, 1965. Although the new Commercial Code makes no changes in the requirements of a valid pledge, we will discuss the law as of September 28, 1964, and show that the transfer of the Diedrich and Shrader note to Mrs. Frasch was valid.

> This transfer had the essential elements of a pledge, which have been said to be: the existence of a debt or obligation, and the transfer of property to be held as security."
>
> 39 Cal. Jur. 2d 502.

See

> Collier on Bankruptcy, No. 4, 14th Ed. 1686.

It was accomplished by the usual method of effectively transferring a chose in action.

> ". . . where a chose in action is represented by a written, such as a note, bill of exchange, . . . delivery of the instrument is effective."
>
> 1 Witkin, Summary of California Law 650;
>
> Rest. Security §§ 1, 2;
>
> *Clark v. Western Feeding Company,* 10 Cal. App. 2d 727, 52 P. 2d 991;
>
> *Reynolds v. Reynolds,* 54 Cal. 2d 669, 355 P. 2d 481.

With Bills and Notes, as in the case of other instruments, the title of the transferor may be conveyed by an assignment in a separate instrument, on the instrument itself, or *by mere delivery.*

> 8 Cal. Jur. 2d 383;
>
> *Vance v. Gilbert,* 178 Cal. 574, 174 P. 42;
>
> *Cassetta v. Baima,* 106 Cal. App. 196, 288 P. 830.

So whether or not the Diedrich-Shrader note was endorsed, the physical transfer of it was enough to constitute a pledge. Neither a writing nor recordation is necessary to constitute a pledge.

> 1 Witkin, Summary of California Law 649.

An assignment of a beneficial interest under a trust deed may be recorded, but a recording is not essential to the completed transfer, and the assignment of a debt carries with it any mortgage or trust deed securing it.

33 Cal. Jur. 2d 674, 678.

B-2. The Uniform Commercial Code as adopted in California January 1, 1965, makes no changes in these requirements.

References to Code Sections hereafter are to the California Commercial Code.

The Code infers that where a security interest is perfected, it takes precedence over the rights of trustees in bankruptcy.

3 California Commercial Law, C.E.B. 97 et seq.

According to § 9301 U.C.C. Comment (1) "perfected" is derived from Bankruptcy Act § 60 (11 U.S.C. 96) in which the term perfected is used to describe a security interest in personal property which cannot be defeated in insolvency proceedings.

A security interest must first attach, under § 9204 (1) and meet the formalities of § 9203(1).

A security interest attaches under § 9204(1) when there is an agreement that it attaches, and value is given, and the debtor has rights in the collateral.

All of these elements are admitted by the pleadings and the findings of fact. (R. 2; R. 27) Mrs. Frasch gave value, $7,000.00. The bankrupts had rights in the notes and trust deed given them by Diedrich and Shrader, and they agreed that it attached by depositing the note and trust deed with Mrs. Frasch.

Under § 9203(1) the formal requisites are met under § 9203(1)(a) when the collateral is in the possession of the secured party. The collateral was in the possession of Mrs. Frasch. (R. 2)

Under § 9203(1)(a) no written security agreement is required for the enforceability of a security interest when the secured party takes possession of the collateral, as in the familiar pledge transaction.

3 California Commercial Law, C.E.B. 54.

B-3. To complete perfection of her interest in the pledged note and trust deed, Mrs. Frasch did not have to file a financing statement.

Section 9302 in pertinent part reads as follows:

> "§ 9302. When Filing Is Required to Perfect Security Interest; Security Interests to Which Filing Provisions of This Division Do Not Apply. (1) A financing statement must be filed to perfect all security interests except the following:
>
> (a) A security interest in possession of the secured party under Section 9305."

Section 9305 in pertinent part reads as follows:

> "When Possession by Secured Party Perfects Security Without Filing. A security interest in . . . goods, instruments, negotiable documents or chattel paper may be perfected by the secured party's taking possession of the collateral."

The California Commercial Code Comment under § 9305 states:

> "The Commercial Code retains the common law idea of perfecting a security interest by possession. Under this section a security interest can

> be perfected by transfer of possession when the collateral is goods, instruments, documents or chattel paper."

The Uniform Commercial Code under § 9305 Comment states:

> "As under the common law of pledge, no filing is required by this Article to perfect a security interest where the secured party has possession of the collateral."

Therefore, since Mrs. Rasch had possession of the Diedrich and Shrader note and held it as security in the form of a pledge, it was not necessary for her to file a financing statement in order to perfect her interest.

Despite the abundant clarity of these sections, the trustee in bankruptcy has taken the position that:

> "Said transfer of said note and deed of trust by the bankrupt to respondent for collateral security constitutes a secured transaction as defined in the California Commercial Code and required the filing of a continuation statement pursuant to Section 10102(c) of the California Commercial Code, which continuation was not filed." (R. 2)

But what does Section 10102(c) say?

In pertinent part it states:

> "Provision for Transition: Continuation Statement. . . . the perfection of a security interest . . . (c) which was perfected when this act takes effect without any filing or recording, but with respect to which a financing statement is required to be filed in order for it to be perfected under

> this code, continues until and will lapse 12 months after this code takes effect; unless, in each case a continuation statement is filed by the secured party within 12 months before the perfection of the security interest would otherwise lapse."

So the section makes the requirement of filing a continuation statement entirely dependent on the security interest being one

> "with respect to which a financing statement is required to be filed in order for it to be perfected under this act . . ."

As is obvious from the sections of the act already quoted, a pledge of a note and trust deed does not require the filing of a financing statement under the act.

Since no such filing is required, § 10102(c) has no application to the facts of this case.

C. HAVING A PERFECTED INTEREST IN THE NOTE AND TRUST DEED, MRS. FRASCH IS A SECURED CREDITOR AND HER LIEN AGAINST THE PLEDGED NOTE AND TRUST DEED IS GOOD AND VALID, AND THE TRUSTEE IS NOT ENTITLED TO THE NOTE AND TRUST DEED UNTIL HE HAS PAID THE DEBT SECURED BY THEIR PLEDGE.

C-1. The appointment of a receiver or trustee in bankruptcy does not deprive the pledgee of his security in accordance with the pledge; its only effect is to inform the receiver or trustee of the amount he must pay in order to redeem the pledged property, and to acquaint him with the amount the pledgee might be

entitled to receive, if anything, out of the general assets, should the security be insufficient to pay the amount due.

International Baking Corp. v. Lynch, 269 Fed. 242.

Where there is a valid pledge, the pledgor's trustee in bankruptcy succeeds to his power of redemption and is entitled to restoration of the pledged property only upon payment of the debt.

Matter of Rogers, 20 Fed. Supp. 120;
M. M. Landy, Inc. v. Nicholas, 221 F.2d 923.

Dated, Bakersfield, California,
January 4, 1968.

Respectfully submitted,
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CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

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